DEPARTMENT OF STATE REVENUE

04-20130271.LOF

Letter of Findings Number: 04-20130271
Sales and Use Tax
For Tax Years 2009-2010

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective as of its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register.

ISSUES

I. Sales and Use Tax–Manufacturing Exemption.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-2.5-5-3; IC § 6-8.1-5-1; Indiana Dep't of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520 (Ind. 1983); Mumma Bros. Drilling Co. v. Department of Revenue, 411 N.E.2d 676 (Ind. Ct. App. 1980); Indiana Dep't. of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96 (Ind. Ct. App. 1974); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991); 45 IAC 2.2-5-8; Letter of Findings 04-20091045 (Sept. 27, 2010); Letter of Findings 04-20120532 (Jan. 31, 2013).

Taxpayer protests the assessment of use tax on certain of its purchase of a "nitrogen storage tank foundation."

II. Sales and Use Tax–Imposition.

Authority: IC § 6-8.1-5-1; IC § 6-8.1-5-2; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007).

Taxpayer argues that the Department incorrectly included "transactions from prior years."

III. Sales and Use Tax–"Contractor Services."

Authority: IC § 6-2.5-1-1; IC § 6-2.5-1-2; IC § 6-2.5-1-5; IC § 6-2.5-1-24; IC § 6-2.5- 1-27; IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-2.5-4-1; IC § 6-2.5-5-3; IC § 6-2.5-5-8; IC § 6-8.1-5-1; Indiana Dep't of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520 (Ind. 1983); 45 IAC 2.2-1-1; 45 IAC 2.2-3-7; 45 IAC 2.2-4-1; 45 IAC 2.2-4-21; 45 IAC 2.2-4-22; Sales Tax Information Bulletin 60 (July 2006); Letter of Findings 04-20120532 (Jan. 31, 2013).

Taxpayer protests the imposition of use tax on its purchase of certain "contractor services."

STATEMENT OF FACTS

Taxpayer is a manufacturer with one manufacturing location in Indiana. Taxpayer manufactures a variety of products out of corn, including ethyl alcohol, starches, corrugated boxes, textiles, corn oil, and corn germ. The Department conducted an audit review of Taxpayer's business records for the 2009 and 2010 tax years. During the audit, the Department reviewed Taxpayer's capital asset purchases for the 2009 and 2010 tax years. Taxpayer provided the Department its Federal Adjusted Gross Income Tax Depreciation Schedule that included assets that were placed in service during 2009 and 2010. As a result of the audit, the Indiana Department of Revenue ("Department") determined that Taxpayer was due a refund for the 2009 tax year, but owed additional use tax for the 2010 tax year. The Department found that Taxpayer had made a variety of purchases on which sales tax was not paid at the time of purchase nor was use tax remitted to the Department. Taxpayer protested the imposition of use tax related to certain of its capital asset purchases. An administrative hearing was held, and this Letter of Findings results.

I. Sales and Use Tax–Manufacturing Exemption.

DISCUSSION

All tax assessments are prima facie evidence that the Department's claim for the tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b). Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). In general, all purchases of tangible personal property are subject to sales and/or use tax. An exemption from use tax is granted for transactions where sales tax was paid at the time of the purchase pursuant to IC § 6-2.5-3-4. In certain circumstances, additional enumerated exemptions from sales and/or use tax are available.

The Department found that Taxpayer purchased machinery and equipment without paying sales tax at the time of purchase, and assessed use tax on the purchases. Taxpayer asserts its purchase of a "nitrogen storage tank foundation" is exempt under the "manufacturing exemption" in IC § 6-2.5-5-3(b).

Generally, all purchases of tangible personal property by persons engaged in the direct production,

manufacture, fabrication, assembly, or finishing of tangible personal property are taxable. 45 IAC 2.2-5-8(a). A statute which provides a tax exemption, however, is strictly construed against the taxpayer. Indiana Dep't. of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "Exemption statutes are strictly construed because an exemption releases property from the obligation of bearing its fair share of the cost of government." General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991), aff'd 599 N.E.2d 588 (Ind. 1992) (Internal citations omitted). Thus, "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." RCA, 310 N.E.2d at 101. Accordingly, the taxpayer claiming exemption has the burden of showing the terms of the exemption statute are met. General Motors, 578 N.E.2d at 404.

IC § 6-2.5-5-3(b) provides:

> Transactions involving manufacturing machinery, tools, and equipment are exempt from the state gross retail tax if the person acquiring that property acquires it **for direct use in the direct production, manufacture**, fabrication, assembly, extraction, mining, processing, refining, or finishing **of other tangible personal property**. (**Emphasis added**).

Thus, the Legislature granted Indiana manufacturers a sales tax exemption for certain purchases, which are for "direct use in direct production, manufacture . . . of other tangible personal property." In enacting the exemption, the Legislature clearly did not intend to create a global exemption for any and all equipment which a manufacturer purchases for use within its manufacturing facility. "[F]airly read, the exemption was meant to apply to capital equipment that meets the 'double direct' test." Mumma Bros. Drilling Co. v. Department of Revenue, 411 N.E.2d 676, 678 (Ind. Ct. App. 1980). The capital equipment "in order to be exempt, must (1) be directly used by the purchaser and (2) be used in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of tangible personal property." Indiana Dep't. of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520, 525 (Ind. 1983). "[T]he test for directness requires the equipment to have an 'immediate link with the product being 'produced.'" Id. Accordingly, the sales tax exemption is applicable to that equipment which meets the "double direct" test and is "essential and integral" to the manufacture of taxpayer's tangible personal property. General Motors, 578 N.E.2d at 401. The application of Indiana's double-direct manufacturing exemptions often varies based on a determination of when a taxpayer's manufacturing process is considered to have begun and ended.

An exemption applies to manufacturing machinery, tools, and equipment directly used by the purchaser in direct production. 45 IAC 2.2-5-8(a). Machinery, tools, and equipment acquired for "direct use in the direct production" is defined in 45 IAC 2.2-5-8(c) as "manufacturing machinery, tools, and equipment to be directly used by the purchaser in the production process" that have "an immediate effect on the article being produced." Property has "an immediate effect" when it becomes "an essential and integral part of the integrated process which produces tangible personal property." 45 IAC 2.2-5-8(c). 45 IAC 2.2-5-8(d) excludes pre-production and post production activities by providing that "'direct use in the production process' begins at the point of first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its complete form." Therefore, proper application of the exemption requires determining at what point "production" begins and at what point "production" ends.

Further, 45 IAC 2.2-5-8(g) states:

> Machinery, tools, and equipment which are used during the production process and which have an immediate effect upon the article being produced are exempt from tax. Component parts of a unit of machinery or equipment, which unit has an immediate effect on the article being produced, are exempt if such components are an integral part of such manufacturing unit. The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property "has an immediate effect upon the article being produced." Instead, in addition to being essential for one of the above reasons, the property must also be an integral part of an integrated process which produces tangible personal property.

Additionally, 45 IAC 2.2-5-8(j) provides:

> Machinery, tools, and equipment used in managerial sales, research, and development, or other non-operational activities, are not directly used in manufacturing and, therefore, are subject to tax. This category includes, but is not limited to, tangible personal property used in any of the following activities: management and administration; selling and marketing; exhibition of manufactured or processed products; safety or fire prevention equipment which does not have an immediate effect on the product; space heating; ventilation and cooling for general temperature control; illumination; heating equipment for general temperature control; and shipping and loading.

Accordingly, tangible personal property purchased for use in the production of a manufactured good is subject to sales and use tax unless the property used has an immediate effect on and is essential to the production of the marketable good. Thus, it is only the property that has an immediate effect on and is essential to the direct production of a marketable good that is exempt.

Taxpayer's protest letter states:

> The nitrogen storage tank is used to store and circulate nitrogen into the manufacturing process. Nitrogen is

used to mix denaturants and alcohol. The nitrogen and denaturants are integrated into the process and is a required step in order to make certain alcohol products. Thus, these tanks are used directly in production of alcohol and are therefore exempt under IC 6-2.5-5-3.

The item at issue here is the concrete for a "nitrogen storage tank foundation." The invoices provided represent that the materials Taxpayer purchased were concrete and piping. While ordinary building foundations are clearly not eligible for the manufacturing exemption, the foundations that are necessary to support production equipment have been found to qualify for the manufacturing exemption in certain situations. See Letter of Findings 04-20091045 (Sept. 27, 2010), 20101124 Ind. Reg. 045100695NRA (finding that the non-ordinary building foundations in question, which supported production machinery were analogous to the work bench discussed in 45 IAC 2.2-5-8(c) example (2)(E), as supported by IC § 6-1.1-1-11(a)(2)(B) and qualified for the manufacturing exemption.)

Notwithstanding that Taxpayer has not demonstrated what type of foundation is at issue, even if Taxpayer had shown this was not an ordinary building foundation, Taxpayer's foundation would not qualify for the exemption. Taxpayer's foundation supports a "nitrogen storage tank." Taxpayer cites to Letter of Findings 04-20120532 (Jan. 31, 2013), 20130327 Ind. Reg. 045130109NRA, as supporting its position that the "nitrogen storage tank" would qualify for the manufacturing exemption. However, the facts of this Letter of Findings are different than Taxpayer's facts in Letter of Findings 04-20120532. The steel tanks at issue in Letter of Findings 04-20120532 were "mixing tanks,"–i.e., the place where the sodium hydroxide was continuous circulated into the product. The tank at issue here is not a "mixing tank," but is a "storage tank."

As provided above, the court in Cave Stone found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. While the "nitrogen storage tank" may be a necessary part of Taxpayer's manufacturing system, the "nitrogen storage tank" is not machinery that has an immediate effect on the manufactured product. The "nitrogen storage tank" simply functions to store the nitrogen and the piping attached to the tank simply transports the nitrogen, a proposed raw material, before it enters the manufacturing process. Accordingly, the storage and transporting of nitrogen is a pre-production activity and does not fall under the exemption.

FINDING

Accordingly, Taxpayer's protest to the imposition of use tax on its purchase of a "nitrogen storage tank foundation" is respectfully denied.

II. Sales/Use Tax–Imposition.

DISCUSSION

All tax assessments are prima facie evidence that the Department's claim for the tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

The Department's audit found that use tax was due on certain purchases that occurred during 2009 and 2010. The Department used the information that Taxpayer provided from its accounting system and federal depreciation schedules to determine the transaction dates. Taxpayer now maintains that a number of these purchases actually occurred prior to 2009 and, therefore, cannot be included in the audit.

Taxpayer apparently relies on IC § 6-8.1-5-2 in support of the proposition that these transactions occurred outside the three-year statute of limitations. However, the documentation provided does not substantiate this proposition. It is possible that a portion of the relevant assessments are out-of-statute but the Department is unable to accept Taxpayer's bare assertion. Without providing substantial evidence that demonstrates these transactions actually occurred at a date that varies from the dates that Taxpayer used as the acquisition dates for the property–in both its accounting system and in its depreciation schedule–the issue remains ambiguous. Therefore, Taxpayer has not met its burden of proving the assessments are incorrect under IC § 6-8.1-5-1.

FINDING

Taxpayer's protest to the Department's inclusion of "transactions from prior years" is denied.

III. Sales and Use Tax–"Contractor Services."

DISCUSSION

The Department found that Taxpayer purchased tangible personal property without paying sales tax at the time of purchase, and assessed use tax on the purchases. Again, pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed accurate, and the taxpayer bears the burden of proving that an assessment is incorrect.

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires tangible personal property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b). Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). In general, all purchases of tangible personal property are subject to sales and/or use tax. An exemption from use tax is granted for transactions where sales tax was paid at the time

of the purchase pursuant to IC § 6-2.5-3-4. In certain circumstances, additional enumerated exemptions from sales and/or use tax are available.

Taxpayer maintains that the Department incorrectly assessed use tax on its purchases from certain "service contractors:" "Contractor S," "Contractor SC," "Contractor B," "Contractor G," and "Contractor P."

A. "Contractor S."

The Department found that use tax was due on Taxpayer's purchases from "Contractor S" for software. Taxpayer maintains that the invoiced amount from "Contractor S" is for "programming labor" and "software installation" for the software for its scales, and represents a "labor only" service transaction that is not subject to sales and use tax. However, based upon the documentation provided, the transaction in question was not a "labor only" service transaction, but was a transaction for the sale of tangible personal property. Specifically, the transaction represents a transaction for computer software.

IC § 6-2.5-1-27 provides, as follows:

"Tangible personal property" means personal property that:

(1) can be seen, weighed, measured, felt, or touched; or

(2) is in any other manner perceptible to the senses.

The term includes electricity, water, gas, steam, and **prewritten computer software**. (**Emphasis added**.)

"Prewritten computer software" is defined in IC § 6-2.5-1-24, as follows:

Subject to the following provisions, "prewritten computer software" means computer software, including prewritten upgrades, that is not designed and developed by the author or other creator to the specifications of a specific purchaser:

(1) The combining of two (2) or more prewritten computer software programs or prewritten parts of the programs does not cause the combination to be other than prewritten computer software.

(2) Prewritten computer software includes software designed and developed by the author or other creator to the specifications of a specific purchaser when it is sold to a person other than the purchaser.

(3) If a person modifies or enhances computer software of which the person is not the author or creator, the person is considered to be the author or creator only of the person's modifications or enhancements.

(4) Prewritten computer software or a prewritten part of the software that is modified or enhanced to any degree, where the modification or enhancement is designed and developed to the specifications of a specific purchaser, remains prewritten computer software. However, where there is a reasonable, separately stated charge or an invoice or other statement of the price given to the purchaser for such a modification or enhancement, the modification or enhancement is not prewritten computer software.

The statutory definition of "pre-written" or "canned" software includes many elements to consider in determining whether or not particular software was designed and developed to meet the requirements of a particular customer. When the software provider has written similar programs for other customers and uses any elements that were part of programs used for other customers, these programs would be considered "pre-written" or "canned" software. IC § 6-2.5-1-24(1)-(2). IC § 6-2.5-1-24(1) provides that combinations of pieces of canned software result in a total piece of software that is prewritten. Thus, the rearrangement and combination of canned elements of software would constitute pre-written or canned software rather than custom designed software. Under IC § 6-2.5-1-24(4), even modifications to pre-written canned software are not considered custom unless there is a reasonable separate charge.

During the course of the protest, Taxpayer presented the invoice for the transaction with "Contractor S." "Contractor S" is a company that sells scales. The invoice shows one unitary charge for "Programming, software and installation on pc's for new alcohol scale. Programming to follow date flow chart as outlined." Since "Contractor S" is a company that sells scales that need software, then presumably this software is "canned software" that is sold to all its customers. Specifically, since the invoice indicated that "programming [is] to follow date flow chart as outlined," this suggests that there is standard programming that is provided for "Contractor S's" customers. Moreover, if any part of the charge did relate to Taxpayer specific modifications or enhancements to the software, these enhancements cannot be considered "custom software" because the invoice did not provide a separate charge. See IC § 6-2.5-1-24(4) (necessitating that for any custom modification or enhancements of software to be considered as "custom software," they must be "reasonable" and in a "separately stated charge.") Thus, even though some programming may have been required to install the "canned software," without a separate billing that indicate a specific reasonable charge for the modifications, any programming for modifications remains "canned software." Therefore, based upon the documentation presented, Taxpayer is unable to sustain its burden of proving that it received nothing other than "canned software" that is tangible personal property that is properly subject to sales and use tax.

Taxpayer also asserts that, to the extent that the charges represented software installation, they are for labor and therefore are not subject to sales tax. However, pursuant to IC § 6-2.5-1-5(b)(6), only "installation charges that are separately stated on the invoice, bill of sale, or similar document given to the purchaser" are excluded from the amount of gross retail income from a transaction that is subject to sales/use tax.

Moreover, since Taxpayer's invoice was for one unitary amount, any amount included in the charge for installation or other services would be subject to tax. A retail "unitary transaction" is one in which items of personal

property and services are furnished under a single order or agreement and for which a total combined charge or price is calculated. IC § 6-2.5-1-1(a). A unitary transaction includes all items of property and services for which a total combined selling price is computed irrespective of the fact that the cost of services, which would not otherwise be taxable, is included in the selling price. 45 IAC 2.2-1-1(a). Therefore, when services are performed as part of a retail "unitary transaction," they are subject to sales and use tax. IC § 6-2.5-1-2(b).

Alternatively, Taxpayer argues that to the extent the charges in the invoice represent a transaction for tangible personal property, the charges were quoted under one "lump sum" price and are the responsibility of the contractor. Taxpayer cites to Sales Tax Information Bulletin 60 to support its claim.

Since Sales Tax Information Bulletin 60 is guidance the Department issued for "construction contractor" converting "construction materials" into "improvements of realty," presumably Taxpayer is asserting that the software contract should be treated like a "lump sum" contract for an "improvement to realty." However, "construction materials" is defined at 45 IAC 2.2-3-7 as "any tangible personal property to be used for incorporation in or improvement of a facility or structure constituting or becoming part of the land on which such facility or structure is situated." Sales Tax Information Bulletin 60 (July 2006), 20060823 Ind. Reg. 045060287NRA, explains that "'Construction materials' means any tangible personal property intended for incorporation in or improvement to real property. Improvements include both new installations and repairs to existing improvements to real property." Since the "computer software" is not a material that becomes part of real property, then it is not a "construction material" and cannot be part of an "improvement to realty" contract. Thus, since Taxpayer's transaction is not for an "improvement to realty," the Department declines Taxpayer's invitation to extend the treatment allowed for the conversion of construction materials under a lump sum contract to Taxpayer's transaction. Therefore, since the transaction in question involved one unitary price, it is correctly classified as a retail "unitary transaction" and as such is properly subject to sales and use tax, as discussed previously.

Accordingly, Taxpayer's protest to the imposition of use tax for the software transaction with "Contractor S" is respectfully denied.

B. "Contractor SC."

The Department found that use tax was due on Taxpayer's purchases from "Contractor SC" for the materials portion of a time and materials contract for "SMF flooring coating" (p. 6 of the audit report). Taxpayer asserts that the Department's assessment of use tax on the "Contractor SC" purchases is incorrect because "Contractor SC" is a "manufacturing contractor" that is responsible for the tax. Taxpayer cites to Sales Tax Information Bulletin 60 to support its claim. During the hearing process, Taxpayer provided the payment invoices for the transactions in question and an email from an employee of the "Contractor SC" stating that "Contractor SC" pays tax to its material suppliers.

The Department refers to 45 IAC 2.2-4-21, which states:

(a) In general, all sales of tangible personal property are taxable, and all sales of real property are not taxable. The conversion of tangible personal property into realty does not relieve a liability for any owing and unpaid state gross retail tax or use tax with respect to such tangible personal property.

(b) All construction material purchased by a contractor is taxable either at the time of purchase, or if purchased exempt (or otherwise acquired exempt) upon disposition unless the ultimate recipient could have purchased it exempt (See 6- 2.5-5 [45 IAC 2.2-5]).

Additionally, 45 IAC 2.2-3-7, in relevant part, explains:

(a) Contractors. For purposes of this regulation [45 IAC 2.2] "contractor" means any person engaged in converting construction material into realty. The term "contractor" refers to general or prime contractors, subcontractors, and specialty contractors, including but not limited to persons engaged in building, cement work, carpentry, plumbing, heating, electrical work, roofing, wrecking, excavating, plastering, tile and road construction.

(b) Construction material. For purposes of this regulation [45 IAC 2.2], "construction material" means any tangible personal property to be used for incorporation in or improvement of a facility or structure constituting or becoming part of the land on which such facility or structure is situated.

Also, 45 IAC 2.2-4-22(d)-(e), states:

(d) Disposition subject to the state gross retail tax. A contractor-retail merchant has the responsibility to collect the state gross retail tax and to remit such tax to the Department of Revenue whenever he disposes of any construction material in the following manner:

(1) Time and material contract. He converts the construction material into realty on land he does not own and states separately the cost for the construction materials and the cost for the labor and other charges (only the gross proceeds from the sale of the construction material are subject to tax); or

(2) Construction material sold over-the-counter. Over the counter sales of construction materials will be treated as exempt from the state gross retail tax only if the contractor receives a valid exemption certificate issued by the person for whom the construction is being performed or by the customer who purchases over-the-counter, or a direct pay permit issued by the customer who purchases over-the-counter.

(e) Disposition subject to the use tax. With respect to construction material a contractor acquired tax-free, the

contractor is liable for the use tax and must remit such tax (measured on the purchase price) to the Department of Revenue when he disposes of such property in the following manner:

(1) He converts the construction material into realty on land he owns and then sells the improved real estate;

(2) He utilizes the construction material for his own benefit; or

(3) Lump sum contract. He converts the construction material into realty on land he does not own pursuant to a contract that includes all elements of cost in the total contract price.

A disposition under C. [subsection (e)(3) of this section] will be exempt from the use tax if the contractor received a valid exemption certificate from the ultimate purchases (purchaser) or recipient of the construction material (as converted), provided such person could have initially purchased such property exempt from the state gross retail tax.

Generally, in a lump sum contract between a customer and its contractor, the contractor bears responsibility for paying the tax on the construction materials. In a time and materials contract between a customer and its contractor, the contractor acts as a retail merchant and sales or use tax is due from the contractor's customers on the cost of the materials.

Sales Tax Information Bulletin 60 (July 2006), 20060823 Ind. Reg. 045060287NRA, defines a "lump sum contract" as "a contract in which all of the charges are quoted as a single price." On the other hand, a "time and materials contract" is defined as "a contract in which all charges for labor, construction materials and other items are separately stated." Id. "'Construction materials' means any tangible personal property to be used for incorporation in or improvement of a facility or structure constituting or becoming part of realty. Id. "Examples of installations that constitute improvements to realty are: doors, garage doors, garage door openers, windows, cabinets, garbage disposals, water heaters, water softeners, alarms, furnaces, central air conditioning units, gutters, and carpeting." Id.

For these "SMF Floor coating" transactions, the "construction contractor" installed/ converted materials into realty and, therefore, the transactions would qualify as transaction for "improvements to realty." However, based upon the documentation provided, the transactions in question were billed under a time and materials contract. For "improvements to realty" that are billed on a "time and materials" basis, the contractor acts as a retail merchant and sales or use tax is due from the contractor's customers on the cost of the materials under 45 IAC 2.2-4-22(d)(1). The contractor failed to charge sales tax on the materials in this case. Therefore, the Department properly assessed use tax on the materials portion of the contract to Taxpayer, the purchaser.

Taxpayer presented a statement from "Contractor SC's" employee indicating that "Contractor SC" paid sales tax when it purchased the materials used. However, even if that were the case, the "Contractor SC's" wrongful payment of sales tax would not relieve Taxpayer of its obligation to pay the Department the assessed use tax. Taxpayer and "Contractor SC" engaged in a transaction subject to sales and use tax. Taxpayer's obligation to pay sales and use tax arose at the time of Taxpayer's purchase of the items. If "Contractor SC" has incorrectly paid sales tax on tangible personal property that qualified for the exemption for tangible personal property purchased for resale pursuant to IC § 6-2.5-5-8(b), then "Contractor SC" would have the remedy of applying for a refund of any sales taxes that were improperly paid as long as the statute of limitations has not run.

Accordingly, Taxpayer's protest to the imposition of use tax on the materials provided for the "SMF floor coating" transactions by "Contractor SC" is respectfully denied.

C. "Contractor B."

The Department found that use tax was due on Taxpayer's purchases from "Contractor B" for "alcohol loadout winch movers." The invoice reflects one price paid for two motorized trolleys, remote controls, freight for delivering the trolleys and remote controls, installation of the trolleys and remote controls, and start up and operational checks. Taxpayer asserts that, to the extent the charges in the invoice represents a transaction for tangible personal property, the charges were quoted under one "lump sum" price and are the responsibility of the contractor. Taxpayer cites to Sales Tax Information Bulletin 60 to support its claim.

Since Sales Tax Information Bulletin 60 is guidance the Department issued for "construction contractor" converting "construction materials" into "improvements of realty," presumably Taxpayer is asserting that the "alcohol loadout winch movers" invoice should be treated like a "lump sum" contract for an "improvement to realty."

Sales Tax Information Bulletin 60 (July 2006) (20060823 Ind. Reg. 045060287NRA), explains that an "improvement to realty," occurs when personal property is "incorporated into and becomes a permanent part of the real property." The Bulletin outlines three requirements in determining whether the use of the personal property is considered an "improvement to realty." Id. The Bulletin states that the personal property must be immovable, annexed, adapted, and become "a permanent part of the land so that it would pass with the land upon a sale." Id. The Bulletin also provides the follow examples of what is and is not a "construction material" for an "improvement to realty," as follows:

"Construction materials" means any tangible personal property intended for incorporation in or improvement to real property. Improvements include both new installations and repairs to existing improvements to real property.

Examples of improvements or repairs to real property are: doors, garage doors, garage door openers, windows, cabinets, garbage disposals, water heaters, water softeners, alarms, furnaces, central air conditioning units, gutters, carpeting and fencing.

Examples of items which are not improvements or repairs to real property are: personal computers, home stereos, televisions, refrigerators, stoves, dishwashers, garbage compactors, clothes washers and dryers and window air conditioning units.

The "alcohol loadout winch movers" do not meet the three requirements outlined in Information Bulletin 60. They were neither immovable, annexed, adapted, nor became "a permanent part of the land so that it would pass with the land upon a sale." Although, for the sake of argument, the "alcohol loadout winch movers" were temporarily mounted to the outdoor structures that are on the land, they could be removed and separately sold, disposed of, or removed at the Taxpayer's choice and did not become "a permanent part of the land so that it would pass with the land upon a sale."

Since the "alcohol loadout winch movers" are not "construction materials" that become part of the real property, then the invoice for their installation cannot be construed as an "improvement to realty" contract. Thus, since Taxpayer's transaction is not for an "improvement to realty," the Department declines Taxpayer's invitation to extend the treatment allowed for the conversion of construction materials under a lump sum contract to Taxpayer's transaction. Therefore, since the transaction in question involved one unitary price, it is correctly classified as a retail "unitary transaction."

Since Taxpayer's invoice was for one unitary amount, any amount included in the charge for installation or other services would be subject to tax. A retail "unitary transaction" is one in which items of personal property and services are furnished under a single order or agreement and for which a total combined charge or price is calculated. IC § 6-2.5-1-1(a). A unitary transaction includes all items of property and services for which a total combined selling price is computed irrespective of the fact that the cost of services, which would not otherwise be taxable, is included in the selling price. 45 IAC 2.2-1-1(a). Therefore, when services are performed as part of a retail "unitary transaction," they are subject to sales and use tax. IC § 6-2.5-1-2(b).

Accordingly, Taxpayer's protest to the imposition of use tax for the "alcohol loadout winch movers" transaction with "Contractor B" is respectfully denied.

D. "Contractor G."

The Department found that use tax was due on Taxpayer's purchases from "Contractor G" for a "peak access catwalk." The invoice reflects one price paid for the "fabrication" of a "catwalk to access 105 Bin." Taxpayer asserts that, to the extent the charges in the invoice represents a transaction for tangible personal property, the charges were quoted under one "lump sum" price and are the responsibility of the contractor. Taxpayer cites to Sales Tax Information Bulletin 60 to support its claim.

First, the "catwalk" would not meet the three requirements–for the use of the personal property to be is considered an "improvement to realty"–that are outlined in the Information Bulletin 60, as previously provided. The "catwalk" were neither immovable, annexed, adapted, nor became "a permanent part of the land so that it would pass with the land upon a sale." Although, for the sake of argument, the "catwalk" was temporarily mounted to the outdoor structures that are on the land, they could be removed and separately sold, disposed of, or removed at the Taxpayer's choice and did not become "a permanent part of the land so that it would pass with the land upon a sale."

Since the "catwalk" is not "construction materials" that become part of the real property, then an invoice for the catwalk's installation cannot be construed as an "improvement to realty" contract. Thus, since Taxpayer's transaction is not for an "improvement to realty," the Department declines Taxpayer's invitation to extend the treatment allowed for the conversion of construction materials under a lump sum contract to Taxpayer's transaction.

Notwithstanding, that Taxpayer documentation demonstrated that the "catwalk" would not be considered a "construction material" that can be installed/converted in an "improvement to realty," this invoice is a contract for the fabrication of the "catwalk" itself. The documentation presented by Taxpayer demonstrates that this invoice, at issue, was for the actual "catwalk." The documentation presented demonstrates that a separate amount was billed for the installation of the "catwalk" (see invoice 21743), which is not at issue here as a tax assessment was not made on this amount for separately stated installation. 45 IAC 2.2-4-21 states that "[t]he conversion of tangible personal property into realty does not relieve a liability for any owing and unpaid state gross retail tax or use tax with respect to such tangible personal property."

Since this amount charged is for the fabrication of the "catwalk," the entire amount charged for the "fabrication of the catwalk" is what is subject to sales and use tax. Pursuant to IC § 6-2.5-4-1(e), the amount of the retail transaction that is subject to sales and use tax includes "the price of the property transferred" and "any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records." (Emphasis added). Further, 45 IAC 2.2-4-1(b)(3) states that the amount of the retail transaction that is subject to tax includes the amounts collected for "services performed or work done on behalf of the seller prior to transfer of such property at retail." Therefore, the Department properly

assessed use tax on Taxpayer's purchase of the "catwalk" from "Contractor G."

Accordingly, Taxpayer's protest to the imposition of use tax for the "peak access catwalk" transaction with "Contractor G" is respectfully denied.

E. "Contractor P" and "Contractor R."

The Department found that use tax was due on Taxpayer's purchases from "Contractor P" and "Contractor R" for a "IPA storage tank foundation" in the amount of $73,618. The invoices presented that represent this $73,618 for this entry demonstrate that Taxpayer actually purchased an "IPA storage tank" from "Contractor P" and an "IPA storage tank foundation" from Contractor R." The first invoice demonstrates that Taxpayer was charged $68,475 for a "12'dia x 16' tall ss304 Denaturant tank." The second invoice demonstrates that Taxpayer was charged $7,973.93, with the materials and labor stated separately, for "construction of a tank foundation." Taxpayer asserts that, to the extent the charges in the invoices represents a transaction for tangible personal property, the charges were quoted under one "lump sum" price and are the responsibility of the contractor. Taxpayer cites to Sales Tax Information Bulletin 60 to support its claim.

1. "IPA Storage Tank" Invoice.

First, the "IPA storage tank" would not meet the three requirements–for the use of the personal property to be is considered an "improvement to realty"–that are outlined in Information Bulletin 60, as previously provided. The "IPA storage tank" is not immovable, annexed, adapted, and became "a permanent part of the land so that it would pass with the land upon a sale." The "IPA storage tank" can be removed and separately sold, disposed of, or removed at the Taxpayer's choice and did not become "a permanent part of the land so that it would pass with the land upon a sale."

Since the "IPA storage tank" is not "construction materials" that became part of the real property, then an invoice for the "IPA storage tank" installation cannot be construed as an "improvement to realty" contract. Thus, since Taxpayer's transaction is not for an "improvement to realty," the Department declines Taxpayer's invitation to extend the treatment allowed for the conversion of construction materials under a lump sum contract to Taxpayer's transaction.

Notwithstanding that Taxpayer's documentation demonstrated that the "IPA storage tank" would not be considered a "construction material" that can be installed/converted in an "improvement to realty," this invoice is a contract for, at best, the fabrication of the "IPA storage tank" itself. The documentation presented by Taxpayer demonstrates that this invoice, at issue, was for the actual "IPA storage tank." 45 IAC 2.2-4-21 states that "[t]he conversion of tangible personal property into realty does not relieve a liability for any owing and unpaid state gross retail tax or use tax with respect to such tangible personal property."

Since the amount charged is for the "IPA storage tank," the entire amount charged for the "IPA storage tank" is what is subject to sales and use tax. Pursuant to IC § 6-2.5-4-1(e), the amount of the retail transaction that is subject to sales and use tax includes "the price of the property transferred" and "any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records." Further, 45 IAC 2.2-4-1(b)(3) states that the amount of the retail transaction that is subject to tax includes the amounts collected for "services performed or work done on behalf of the seller prior to transfer of such property at retail." Therefore, the Department properly assessed use tax on Taxpayer's purchase of the "IPA storage tank" from "Contractor P."

Alternative, Taxpayer argues that, to the extent the charges for the "IPA storage tank" represent a transaction for tangible personal property, this purchase qualifies for the "manufacturing exemption" under IC § 6-2.5-5-3. Taxpayer cites to Letter of Findings 04-20120532 (Jan. 31, 2013), 20130327 Ind. Reg. 045130109NRA, as supporting its position that the "IPA storage tank" would qualify for the manufacturing exemption.

However, the facts of this Letter of Findings are different than Taxpayer's facts in Letter of Findings 04-20120532. The steel tanks at issue in Letter of Findings 04-20120532 were "mixing tanks,"–i.e., the place where the sodium hydroxide was continuous circulated into the product. The tank at issue here is not a "mixing tank," but is a "storage tank." As provided above in Issue I, the court in Cave Stone found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. While the "IPA storage tank" may be a necessary part of Taxpayer's manufacturing system, the "IPA storage tank" is not machinery that has an immediate effect on the manufactured product. The "IPA storage tank" simply functions to store the denaturant, a proposed raw material, before it enters the manufacturing process. Accordingly, the storage of denaturant is a pre-production activity and does not fall under the exemption.

Accordingly, Taxpayer's protest to the imposition of use tax for the "IPA storage tank" transaction with "Contractor P" is respectfully denied.

2. "IPA Storage Tank Foundation" Invoice.

Based upon the pictures and documentation presented, the "IPA storage tank foundation" would meet the three requirements–for the use of the personal property to be considered an "improvement to realty"–that are outlined in the Information Bulletin 60, as previously provided. The "IPA storage tank foundation" is immovable, annexed, adapted, and became "a permanent part of the land so that it would pass with the land upon a sale."

The "IPA storage tank foundation" cannot be removed and separately sold, disposed of, or removed at the Taxpayer's choice and would become "a permanent part of the land so that it would pass with the land upon a sale." Therefore, the "Contractor R" installed/ converted materials into realty, and the transactions would qualify as transaction for "improvements to realty."

However, based upon the invoice provided, "Contractor R" billed the transaction in question were under a time and materials contract. For "improvements to realty" that are billed on a "time and materials" basis, the contractor acts as a retail merchant and sales or use tax is due from the contractor's customers on the cost of the materials under 45 IAC 2.2-4-22(d)(1). The contractor failed to charge sales tax on the materials in this case. Thus, the Department would have properly assessed use tax on the materials portion of the contract to Taxpayer, the purchaser. However, the entire $7,973.93 of the invoice was included in the amount subject to tax and only the $5,143.93 that relates to the materials should have been included.

Accordingly, Taxpayer's protest to the imposition of use tax on the "IPA storage tank foundation" is sustained in part in the amount of $2,800 of taxable purchases, which represents the labor portions of invoice number 92010-2.

FINDING

Taxpayer's protest is denied in part and sustained in part. Taxpayer's protest to the imposition of use tax on the "IPA storage tank foundation" (on p. 6 of the audit report) is sustained in the amount of $2,800 of taxable purchases which represents the labor portions of invoice number 92010-2, as discussed in subpart E(2). However, Taxpayer's protest to the imposition of tax on all the other purchases is denied.

SUMMARY

Taxpayer's protest is denied in part and sustained in part. Taxpayer's protest to the imposition of use tax on the "IPA storage tank foundation" (on p. 6 of the audit report) is sustained in the amount of $2,800 of taxable purchases which represents the labor portions of invoice number 92010-2, as discussed in Issue III subpart E(2). However, Taxpayer's protest to the imposition of tax on all the other purchases is denied.

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